



U.S. Department of Housing and Urban Development

District Office of the Inspector General
Office of Audit
Richard B. Russell Federal Building
75 Spring Street, SW, Room 700
Atlanta, GA 30303-3388
(404) 331-3369

April 17, 1997

Audit Related Memorandum

No. 97-AT-205-1806

MEMORANDUM FOR: Harold Saether, Director, Public Housing Division, 4APH

FROM: Nancy H. Cooper
District Inspector General for Audit-Southeast/Caribbean, 4AGA

SUBJECT: Limited Review of Martin Street Plaza
Atlanta, Georgia

INTRODUCTION AND SCOPE

We conducted a limited review of the renovation of Martin Street Plaza apartments to determine whether Department of Housing and Urban Development (HUD) funds were properly drawn and expended as authorized for the grant period from October 28, 1994 through October 27, 1997. Our review focused on expenditures and performance of Charis Community Housing, a non-profit organization that received a \$900,000 HOPE I technical assistance grant to oversee the conversion of Martin Street Plaza from public housing to homeownership units. Charis was responsible to assist and advise the residents, assist the Atlanta Housing Authority (AHA) in monitoring the construction, and financially manage over \$2.9 million in grants and donated funds to be used for project renovation, job training, and resident job and business development. HUD was responsible for monitoring Charis' performance, reviewing draw requests, and providing technical assistance. We conducted our review from September 1996 to March 1997.

SUMMARY OF AUDIT RESULTS

Charis did not maintain control over the finances of Martin Street Plaza. Charis did not support or follow its cost allocation plan, paid ineligible labor costs from HOPE I grant funds, did not support overhead costs, charged donated materials to the comprehensive grant, made inaccurate accounting entries, and did not support its HOPE I draw requests. These deficiencies occurred because of the complexity of Charis' accounting system coupled with its lack of written accounting policies and procedures. Charis was unable to account for the \$1.7 million drawn as of November 1996 on activities at Martin Street Plaza, and we were therefore unable to determine the reasonableness and necessity of grant expenditures. To the extent we were able

to perform audit tests, we identified \$68,826 in ineligible costs. Until Charis reconciles its accounting records and produces support for charges and grant draws, we consider all \$1.7 million to be unsupported.

We concluded that Charis had provided training, technical assistance, and counseling to Martin Street Plaza tenants as required in the HOPE I grant agreement. Charis provided various forms of training to tenants during rehabilitation through on-the-job apprenticeship training, attendance at conferences, and skill assessments.

We also concluded that Charis monitored the contractor and took timely action to address problems -- to the extent it was authorized. Documentation showed that Charis began warning the AHA, who had primary responsibility to monitor the construction, of the contractor's failure to perform prior to April 1996.

We did not review the quality of rehabilitation work because the AHA had determined the work to be deficient and had obtained a settlement with the general contractor's bonding company.

SUMMARY OF CHARIS' COMMENTS

We discussed our results with Charis officials during the audit and at an exit conference held on March 17, 1997. Charis took responsibility for accounting errors regarding incorrect salary allocation, improper labor charges, incorrect accounting entries, and unsupported draw requests. Charis disagreed that donated materials were improperly charged to the comprehensive grant. Also, Charis believed HUD did not provide technical assistance needed during the grant and should share the responsibility for the conditions in the report. Charis submitted documentation, which will be considered as part of the resolution of this report, to address some of the accounting deficiencies noted in this report. We revised the report where appropriate, but our recommendations remain unchanged.

Charis submitted written comments on April 10, 1997 to the draft report sent on February 28, 1997. Charis' comments are included as Attachment 2 to this memorandum.

BACKGROUND

Located in the Olympic Stadium venue and Atlanta's Empowerment Zone, the Martin Street Plaza Community organized to rebound from being isolated and economically distressed. The residents formed Martin Street Plaza, Inc., a non-profit community development corporation, focused on the:

- renovation of the Martin Street Plaza apartments,
- creation of permanent jobs for residents, and
- transformation of the 60 unit public housing community into a private homeownership cooperative.

Incorporated in 1993, Martin Street Plaza, Inc. was a charitable organization with 501(c)(3) tax-exempt status. The Board of Directors consisted of 11 Martin Street Plaza residents.

With the assistance of Southern Ministry Network, the Martin Street Plaza leadership organized a public/private partnership with Amoco Corporation, The Home Depot, Charis Community Housing, NationsBank, HUD, the AHA, Georgia Housing Finance Authority (GHFA), and Summerhill Neighborhood Development Corporation (SNDC). The public/private partners provided funds for the renovation and homeownership conversion. In total, the Martin Street Plaza redevelopment was to be funded with over \$3.9 million as follows:

<u>Award Amount</u>	<u>Funds Drawn¹</u>	<u>Source of Award</u>
\$2,000,750	\$526,958	Comprehensive grant funds from HUD awarded through the AHA under three contracts to the joint venture and the general contractor ²
\$900,000	\$703,141	HOPE I Technical Assistance grant awarded by HUD to Charis to provide technical assistance ³
\$600,000	\$471,741	Private donations from The Home Depot and Amoco Foundation
\$245,000	None	GHFA commitment to the tenant based homeownership cooperative
\$100,000	\$50,963	Tenant Opportunity Program (TOP) grant funds awarded by HUD to the Martin Street Plaza tenants' association ⁴
<u>\$75,000</u>	<u>None</u>	Heinz grant awarded by HUD to the tenants' association.
<u>\$3,920,750</u>	<u>\$1,752,803</u>	Totals

The Martin Street Plaza transformation to homeownership was to be accomplished through the joint efforts of Charis, the resident community, the AHA, and HUD. The AHA was responsible for selection and retention of the general contractor who performed the rehabilitation. Charis assisted the AHA in monitoring the general contractor and alerted the AHA to any problems that arose.

¹ As of November 1996.

² Charis was only involved with the \$526,958 drawn on the two contracts awarded for \$975,868 to the joint venture. The remaining comprehensive grant balance of \$1,024,882 was awarded in one contract to Norwest.

³ The HOPE I grant was the primary focus of our review. However, we also reviewed certain transactions from the donor and comprehensive grant funds to better understand HOPE I expenditures.

⁴ We reported on TOP Grant deficiencies in audit report No. 97-AT-101-002, dated February 21, 1997. One deficiency cited was retaining grant fund in excess of immediate needs. Charis confirmed in their written comments to this report that \$21,888 of \$50,963 drawn remained in the bank.

Charis was also responsible for financial management. Charis organized the operations around three separate entities according to the funding awarded.

MSP Development/Charis Community Housing - Charis Community Housing created a separate division called MSP Development to administer the activities of Martin Street Plaza. MSP Development was headed by a grant manager, who was responsible for the daily operations at Martin Street Plaza. For this division, Charis hired an accountant, a secretary, a construction manager, an assistant construction manager and several laborers. Charis also provided on-the-job training to tenants in various positions in this division. Charis tracked donor funds and HOPE I Technical Assistance grant funds under the name of MSP Development.

Martin Street Plaza, Inc./MSP Contracting - The tenants formed a nonprofit organization called Martin Street Plaza, Inc./MSP Contracting. Martin Street Plaza, Inc./MSP Contracting was legally controlled by the tenants, but Charis advised the tenants and administered the daily accounting activities. Four tenant board members had signature authority and responsibility for all transactions, and signed legal documents such as checks usually under Charis' direction. MSP Contracting performed construction work at the project in a joint venture with a private contractor. Charis maintained a separate accounting system for MSP Contracting. Charis also tracked TOP grant funds under this accounting system.

MSP Contracting/Norwest Joint Venture - The AHA selected Norwest to be the general contractor. MSP Contracting and Norwest formed a joint venture of which MSP Contracting owned 51 percent. The AHA awarded contracts to the joint venture to install a security fence and rehabilitate the exterior of the units. The tenants planned to use earnings from the rehabilitation work to match the \$75,000 Heinz grant. One MSP tenant board member had signature authority and responsibility for the transactions of the joint venture and signed legal documents such as checks and grant draws under the direction of Charis. Charis maintained a separate accounting system for the joint venture and tracked costs and earnings associated with the comprehensive grant contracts.

The Martin Street Plaza project faltered around the spring of 1996. After several months of continuous construction problems reported by Charis and the AHA, the AHA removed MSP Contracting and Norwest for nonperformance. This caused the tenants to split their support between Charis and the general contractor. The AHA attempted to resolve the conflict, but was unsuccessful. With the partnership in turmoil, the project stalled with only 26 percent of the comprehensive grant funds drawn for the renovation. Meanwhile, Charis continued to incur salary expenses and had consumed about \$700,000 of the \$900,000 grant by the time we completed our field work in February 1997.

CHARIS DID NOT PROPERLY ACCOUNT FOR DRAWS OF \$1.7 MILLION

Charis failed to properly account for over \$1.7 million drawn for the activities at Martin Street Plaza. Charis did not support or follow its allocation plan, charged ineligible labor costs to the HOPE I grant, did not support overhead costs, charged donated materials to the comprehensive grant, made inaccurate accounting entries, and did not support HOPE I grant draws. We attribute these conditions to an overly complex accounting system and no written accounting policies and procedures. Consequently, we were unable to determine the reasonableness and necessity of HOPE I grant expenditures. To the extent we were able to perform audit tests, we identified a total of \$68,826 in ineligible charges. The remainder of the \$1.7 million was unsupported.

Criteria

Charis was guided by various pronouncements which prescribed its responsibility to maintain accurate accounting records and reports. Office of Management and Budget (OMB) Circular A-110, entitled, "Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations," subpart C section 84.21(b)(3) requires recipients to maintain effective control over and accountability for all funds. Recipients shall adequately safeguard all such assets and assure they are used solely for authorized purposes. OMB Circular A-122, entitled "Cost Principles for Nonprofit Organizations," Attachment B, paragraph 23 states the costs of materials and supplies necessary to carry out an award are allowable. Such costs should be charged at their actual prices after deducting all cash discounts, rebates, and allowances received by the organization.

The HOPE I technical assistance grant agreement (Article VII) required Charis to keep records that would facilitate an effective audit, demonstrate compliance with program requirements, fully disclose the amount and disposition by the recipient of the grant funds received, document the reasonableness and necessity of each expenditure, and accumulate the total cost for the technical assistance program.

Cost allocation plan not supported or followed

Charis did not support its allocation of employee salaries and benefits to the various funding sources. Charis established an allocation plan to distribute salaries among the HOPE I technical assistance grant, the TOP grant, MSP Contracting account, and donor account. Generally, the plan called for allocation to four funding sources at different rates depending upon the job position. For example, the accountant's salary was to be charged at one-third each to TOP, HOPE I, and MSP Contracting. However, employees did not show the actual allocation of their time among different grants and activities on their time sheets to support these rates.

Furthermore, Charis did not always allocate expenses according to the plan. Except for May 1996, Charis charged all MSP related salaries incurred after March 1996 to the HOPE I grant. We identified at least \$53,296 in ineligible salary costs in our test period from January 1996 to August 1996. In addition, Charis charged all MSP related employee health benefit costs for the entire grant period to the HOPE I grant. We noted discrepancies such as these throughout the entire grant period, but due to the poor condition of accounting records, we did not attempt to calculate the total ineligible amounts charged against the HOPE I grant.

Ineligible labor costs charged to the HOPE I grant

Charis paid labor costs of at least \$44,488 from HOPE I grant funds for renovation work from January 1996 through August 1996. The joint venture was responsible for these costs and had already drawn comprehensive grant funds to cover these payments. The joint venture should have returned the \$44,488 to Charis but never did. The grant manager stated Charis inadvertently charged the HOPE I grant for the wages of laborers working under the comprehensive grant. Charis had not established written policies and procedures that directed the Charis accounting personnel on the proper treatment of labor wages.

HOPE I grant overhead costs not supported

Charis had no support for \$70,000 drawn for overhead costs. Charis retained \$35,000 and paid \$35,000 to SNDC. Charis did not realize overhead costs had to be supported and simply drew these amounts based on what was budgeted in the grant agreement.

Charis budgeted a total of \$105,000 for overhead to be shared equally by Charis, the AHA, and SNDC. Charis was required by the grant agreement to execute subgrant agreements with the AHA and SNDC before disbursing any funds to them. However, Charis never executed subgrant agreements. Charis had no support for the \$35,000 paid to SNDC, and we could not determine what services SNDC provided. Also, we found no support for the \$35,000 retained by Charis for overhead.

Charis did not reimburse the AHA for overhead. Instead, Charis used the money to provide security at Martin Street Plaza as directed by the AHA. Charis improperly recorded the costs as "AHA Overhead," but the amounts were otherwise supported by documentation.

Value of donated materials charged to the comprehensive grant

The joint venture drew at least \$24,338 of comprehensive grant funds to reimburse MSP Contracting for building materials that, we determined, had been donated by The Home Depot. These draws were flagrantly improper because no costs were incurred. Charis officials directed the joint venture to bill the comprehensive grant for the value of the donated materials, then transfer the cash to MSP Contracting where it was to be used for other project purposes. We confirmed Charis transferred these funds to MSP Contracting, but we were unable to determine how the funds were used by MSP Contracting.

In addition, Charis recorded another \$54,830 in accounts payable to MSP Contracting in the joint venture's accounts for other donated materials. Because the grant draws were not properly supported, we could not confirm whether Charis ever drew comprehensive grant funds for these additional donated materials.

Inaccurate accounting entries for HOPE I funds

Charis did not always record expenditures in the appropriate accounting code. Examples of such errors include:

- Payments for payroll taxes were incorrectly posted to each salary line item instead of the payroll taxes and health benefits line item.
- Three expenditures for an IRS tax levy deduction from the grant manager's salary were never posted.
- General liability insurance and a general liability insurance audit were incorrectly posted.

The independent Certified Public Accountant (CPA), hired by Charis to audit the 1994 financial statements, noted similar problems. In a letter dated June 2, 1995, the CPA notified Charis of several issues that needed to be addressed, including the proper classification of costs.

"Accounting should be responsible for the coding of the invoices and P.O.'s (purchase orders). However, they must be provided with sufficient information to determine where the expenditures should be coded. This should be provided by the individual responsible for approving the expenditure for payment. Improper coding of items can create areas reflected as over budget when they are not. Unnecessary questions or requests for reclassification from HUD can be avoided by proper coding."

Charis had not established written policies and procedures to instruct accounting employees in the proper treatment of such expenditures. As a result, the general ledger accounts were inaccurate and unreliable. We could not determine the actual amounts expended for each line item without retracing and correcting all transactions during the grant period.

HOPE I grant draw requests not supported

Charis did not make draw requests based on actual expenditures. Instead, they drew funds according to the line item budget established in the grant application, then used the funds for any expenditure as it came due. We compared draw requests to actual expenditures for the budget line item for payroll taxes and health benefits. Charis drew only \$54,206 for this line item for the 21 months from November 1994 through July 1996. However, actual expenditures for health benefits alone in just the first 7 months of 1996 amounted to over \$58,600.

The CPA addressed the reconciliation of draw requests in the same June 2, 1995 letter mentioned above.

"At year end, with only a few expenditures occurring, it has been extremely time consuming to reconcile the requests for funds with the expenditures recorded in the general ledger. This will become an even greater problem in 1995 as the volume of expenditures increase. Therefore, this reconciliation should be implemented immediately."

Charis never implemented the reconciliation procedure suggested by its CPA firm. We could not reconcile the draw requests with actual expenditures without retracing all transactions during the grant period.

Charis' response to the draft report

Charis took responsibility for certain accounting errors regarding the accounting practices for Martin Street Plaza. Charis disagreed with the presentation that \$1.7 million was not properly accounted for. Charis stated the \$526,958 in comprehensive grant funds was not their responsibility because it was awarded through the AHA to the joint venture. In addition, Charis claimed to have corrected its accounting records to show an accounting for all of the HOPE I grant funds.

In an effort to correct the accounting errors for the HOPE I grant, Charis computed the total ineligible salary and labor costs charged to the HOPE I grant for 1996 as \$79,159 (our total was \$97,784). Charis stated it, "did not take these funds for its own use, but the MSP-related accountant simply failed to allocate these expenses to the appropriate funding sources, causing the HOPE I grant to pay for all these expenses."

Charis does not agree that it is responsible for repaying the \$24,338 billed to the Federal grant for donated goods. Charis contended the donated materials obtained by MSP Contracting from The Home Depot could be sold to any third party at cost. The selling of these materials to the joint venture was simply a way to provide funds to enable the residents to establish their resident-based businesses. This is a business transaction between MSP Contracting, Inc. and the joint venture that does not involve HUD funds and is outside of HUD's jurisdiction. Further, Charis stated the arrangement was known to all parties involved and verbally communicated to HUD.

Charis officials stated that the responsibility for the conditions cited in the report should be shared by HUD for not providing technical assistance needed during the grant. Charis stated HUD was aware that the HOPE I technical assistance grant was the first of its kind in the country and Charis' first Federal grant. HUD should have monitored more closely. For example, Charis stated HUD did not question the overhead amounts clearly shown on each draw request despite HUD's practice to manually review each request. Charis provided HUD's Office of Public Housing with documentation to support the overhead charges subsequent to completion of our field work.

Evaluation of Charis' comments

We consider Charis responsible for the \$1.7 million because Charis advised or directed the tenants in conducting the joint venture business and Charis maintained the joint venture's accounting records. Charis still needs to account for the \$526,958 in comprehensive grant funds, the \$471,741 in donor funds, and the \$50,963 in TOP grant funds. The deficiencies described in this report show the condition of the books and records at the time of our field work. We have not audited the documents submitted with Charis' response to the draft report.

Our review showed unsupported salary charges of \$53,296 and ineligible labor charges of \$44,488 for a total of \$97,784. We did not verify the accuracy of the \$79,159 computed by Charis nor the adequacy of the documentation submitted to HUD's Office of Public Housing to support the overhead computation. HUD should review this material in resolution of this report.

HUD comprehensive grant funds were the only funds available to pay MSP Contracting for donated goods. Because Charis advised or directed the tenants on all financial matters and maintained the accounting records for the tenants, we believe Charis is responsible to repay the funds.

We did not review the extent to which HUD assisted the grantee nor whether additional technical assistance would have prevented the accounting conditions cited in this report.

Recommendations:

We recommend that you:

- 1A. Seek support and full accounting for use of the \$1.7 million drawn from the HOPE I grant, donated goods and funds, the TOP grant, and the comprehensive grant; review the accuracy and adequacy of the corrections made since our field work for the HOPE I grant expenditures; and prohibit Charis from participating in other HUD programs if it is unable to properly account for these expenditures.
- 1B. Require Charis to justify its methodology for the \$53,296 charged to the HOPE I grant contrary to the allocation plan or seek reimbursement for the improperly allocated salaries.
- 1C. Seek reimbursement for the ineligible contract labor costs of \$44,488 charged to the HOPE I grant.
- 1D. Obtain support for the \$70,000 in overhead costs or seek reimbursement.
- 1E. Require Charis to repay the \$24,338 transferred to MSP Contracting for donated goods.
- 1F. Require Charis to correct accounting entries in the accounting records for Martin Street Plaza, including those related to the salaries, payroll taxes, and health benefits.
- 1G. Require Charis to reconcile HOPE I grant draw requests to expenditures.
- 1H. Require Charis to obtain an audit for 1996.

SCHEDULE OF INELIGIBLE AND UNSUPPORTED COSTS

<u>Recommendation</u>	<u>Amount Ineligible⁵</u>	<u>Amount Unsupported⁶</u>
1A		\$ 1,752,803
1B		53,296
1C	\$ 44,488	
1D		70,000
1E	<u>24,338</u>	<u> </u>
Total	<u>\$ 68,826</u>	<u>\$ 1,876,099⁷</u>

⁵ Ineligible amounts obviously violate law, contract, HUD or local agency policies or regulations.

⁶ Costs not clearly eligible or ineligible but warrant being contested.

⁷ The total includes a duplicated amount of \$123,296 for recommendations 1B and 1D.

DISTRIBUTION

Secretary's Representative, 4AS
Director, Office of Public Housing, 4APH
Audit Liaison Officer, 3AFI
Director, Field Accounting Division, 4AFF
Chief Financial Officer, F, (Room 10164) (2)
Deputy Chief Financial Officer for Finance, FF, (Room 10164) (2)
Director, Housing and Community Development, Issue Area, US GAO
 ATTN: Judy England-Joseph
Audit Liaison Officer, Office of Public and Indian Housing, PF (Room 4122) (3)
Assistant to the Deputy Secretary for Field Management, SDF (Room 7106)
President, FCS Urban Ministries
Executive Director, Charis Community Housing
President, Martin Street Plaza Board of Directors
Renee Glover, Executive Director, Atlanta Housing Authority